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Puerto Rico

Revised Plan Proposals From PROMESA Oversight Board, PSA Creditors Would Increase Cash Consideration by $2B, Lower Cap on Maximum Annual Debt Service; Proposals Differ Over Composition of Total Consideration

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Relevant Documents:
Aug. 24 PSA Proposal (PSA Creditors)
Aug. 18 Plan Proposal (Oversight Board)

A revised commonwealth plan of adjustment proposed by the PROMESA oversight board and a counterproposal by the principal creditor parties to the commonwealth plan support agreement both call for a $2 billion increase in cash consideration for general obligation/Public Buildings Authority bondholders and lower caps on maximum annual debt service compared with the existing PSA struck in February. Both proposals, which date back to August, were disclosed late Wednesday amid ongoing debt restructuring negotiations and court-directed mediation under Title III of PROMESA.

As outlined below in a comparison prepared by the PSA parties, although both proposals contemplate total cash of $5.984 billion, reflecting a $2 billion increase from the existing PSA, the blended GO/PBA recovery under the oversight board's proposal based on claims net of original issue discount, or OID, would range from 52.7% to 58.4%, while the PSA creditors' proposal contemplates a blended recovery based on such claims net of OID at 73.6%. The total consideration under the oversight board's proposal includes bonds in an amount between $4.993 billion and $5.22 billion, while the PSA creditors' counterproposal contemplates $7.406 billion of bonds and $611 million of "SUT Equity":

SIDE-BY-SIDE SUMMARY

	FEBRUARY 9, 2020 PSA	JULY 30, 2020 FOMB PROPOSAL	AUGUST 24, 2020 PSA CREDITORS PROPOSAL
PROPOSAL PARTIES	▪ FOMB ▪ LCDC ▪ QTCB Noteholder Group ▪ Ad Hoc Group of Constitutional Debtholders ▪ Ad Hoc Group of General Obligation Bondholders	▪ FOMB	▪ LCDC ▪ QTCB Noteholder Group ▪ Ad Hoc Group of Constitutional Debtholders ▪ Ad Hoc Group of General Obligation Bondholders
TOTAL CONSIDERATION	▪ $14,478MM, consisting of: – $10,669MM bonds – $3,809MM cash	▪ $10,976MM - $11,204MM, consisting of: – $4,993MM - $5,220MM bonds(1) – $5,984MM cash	▪ $14,001MM, consisting of: – $7,406MM bonds – $5,984MM cash – $611MM 5.5% SUT Equity(2)
BASE CONSIDERATION TO GO / PBA	▪ $13,551MM, consisting of: – $10,142MM bonds – $3,409MM cash	▪ $10,526MM - $10,754MM, consisting of: – $4,943MM - $5,170MM bonds(1) – $5,584MM cash	▪ $13,551MM, consisting of: – $7,356MM bonds – $5,584MM cash – $611MM 5.5% SUT Equity(2)
BASE CONSIDERATION TO NON-GO / PBA	▪ $527MM bonds	▪ $50MM bonds	▪ $50MM bonds
BLENDED GO / PBA RECOVERY(3)	▪ Based on claims gross of OID: 72.2% ▪ Based on claims net of OID: 73.6%	▪ Based on claims gross of OID: 56.1% - 57.3% ▪ Based on claims net of OID: 57.2% - 58.4%	▪ Based on claims gross of OID: 72.2% ▪ Based on claims net of OID: 73.6%
PBA OWN-SOURCE RECOVERY	▪ $1,073MM cash	▪ N/A	▪ Same as existing PSA
5.5% SUT EQUITY	▪ N/A	▪ N/A	▪ 5.5% SUT Equity will receive 50% of the difference between the actual 5.5% Pledged SUT collections and 80% of the 5.5% Pledged SUT implied by the May 27, 2020 Certified Fiscal Plan – 5.5% SUT Equity will terminate on July 1, 2040 with no further payment obligations – The Commonwealth cannot change the scope and amount of the 5.5% Pledged SUT. The Commonwealth may not exempt goods from the 5.5% Pledged SUT without providing for substitution of collateral of equal value – New York law and forum – Other terms and conditions subject to agreement – Payment caps TBD

Note: All stated recoveries are calculated on the respective proposal date. All items remain subject to additional diligence.
(1) Range of total debt under the July 30, 2020 FOMB Proposal reflect illustrative max GO and max COFINA Jr. scenarios, respectively.
(2) Represents net present value as of July 1, 2020 using a discount rate of 20% and the projected 5.5% Pledged SUT implied by the May 27, 2020 Certified Fiscal Plan.
(3) Excludes PSA Restriction Fee and Consummation Costs.

The materials disclosed on Wednesday include an Aug. 18 fiscal plan macroeconomic overview and revised plan of adjustment proposal from the oversight board and an Aug. 24 counterproposal from PSA creditors including the Lawful Constitutional Debt Coalition, or LCDC, the QTCB noteholder group, the ad hoc group of constitutional debtholders, and the ad hoc group of GO bondholders. The counterproposal indicates that the oversight board proposal was floated on July 30.

According to an oversight board press release, notwithstanding the document release, the oversight board and such creditors, holding in excess of $9 billion of the commonwealth's debt, continue to negotiate in an effort to enable Puerto Rico to exit the Title III bankruptcy proceedings as soon as reasonably possible with an agreement to restructure Puerto Rico's debt to a sustainable level.

The existing PSA, executed in connection with the amended plan of adjustment the oversight board filed in February, was sidelined by the Covid-19 pandemic but has not been terminated. The release says that the oversight board will update the Title III court in late October about the status of the negotiations.

The disclosures come on the heels of the official committee of unsecured creditors asking the court to allow the UCC to proceed with its claim objection seeking to determine the priority of GO bonds. Judge Laura Taylor Swain denied the request without prejudice, citing oversight board assurances that plan negotiations were in the works, and indicated that the court's administrative stay related to the UCC claim objection would remain in place until at least March 2021.

Oversight Board Proposal

The oversight board states that its revised proposal was developed to make the plan of adjustment

“sustainable and affordable given the negative effect of the pandemic and economic shutdown” by increasing the amount of cash consideration by nearly $2 billion and reducing maximum annual debt service to $1.05 billion, down from $1.472 billion in the existing plan from February.

The $2 billion increase in the cash consideration, which would rise to $5.984 billion from $3.8 billion, materially derisks securities design elements as compared with the prior plan of adjustment, according to the proposal, adding that the design would be determined in coordination with the commonwealth given the need for related legislation.

Paring annual debt service to $1.05 billion reflects “significantly lower longer term projections,” according to the Aug. 18 proposal, adding that the commonwealth’s liquidity remains “limited” throughout the projection period.

Turning to the share of total consideration for GO bondholders, the proposal contemplates further limiting junior creditor recoveries “given key court cases” in the Title III proceedings regarding the Puerto Rico Highways and Transportation Authority, or HTA, and Employees Retirement System, or ERS. Class recoveries are assumed to be reduced pro rata due to the decline in total consideration, according to the proposal.

Under an item called municipal market outperformance, the proposal notes that while the fiscal outlook for Puerto Rico “remains challenged, tax exempt rates have fallen significantly” since the plan of adjustment was negotiated, adding that the proposal reflects an adjusted coupon structure that could improve secondary market efficiency post-confirmation.

The oversight board document includes the following summary of the revised proposal:

Proposal for Revised Plan of Adjustment

The revised Plan of Adjustment seeks to make the restructuring sustainable and affordable by increasing the amount of cash consideration by nearly $2 billion and reducing maximum annual debt service to $1.05 billion

The FOMB has developed the revised proposal to make the Plan of Adjustment sustainable and affordable given the negative effect of the pandemic and economic shutdown

- Cash: Cash consideration increased by ~$2 billion
  - Materially de-risks securities design elements as compared to the prior Plan of Adjustment
- Maximum Annual Debt Service: Reduced to $1.05 billion, reflecting significantly lower longer-term projections
  - Securities design to be determined in coordination with the Commonwealth, given required legislation
  - Despite lower debt service, the Commonwealth’s liquidity remains limited throughout the projection period
- GO Share of Total Consideration: Junior creditor recoveries further limited given key court cases (i.e., HTA and ERS)
- Class Recoveries: Assumed to be reduced pro-rata for decline in total consideration
- Municipal Market Outperformance: While the fiscal outlook for Puerto Rico remains challenged, tax-exempt rates have fallen significantly since the PoA was negotiated
  - Proposal reflects an adjusted coupon structure that could improve secondary market efficiency post-Confirmation

As illustrated above, the revised proposal contemplates between $4.99 billion and $5.22 billion in new debt, down from approximately $10.7 billion in the existing plan, with related footnotes stating that the “split” between COFINA junior and GO bondholders as well as the coupon structure remain to be determined. The proposed revised plan of adjustment assumes a 20-year term and deemed

issuance date of July 1, 2021.

Total commonwealth consideration, or the new debt and cash consideration combined, would range between $10.976 billion and $11.2 billion in the revised proposal, down from $14.478 billion. Factoring in a $50 million consideration for non-GO/PBA creditors, down from $527 million in the existing plan, and an unchanged $400 million plan support agreement fee, the oversight board's revised proposal would bring the commonwealth consideration available for GO/PBA bondholders to between $10.526 billion and $10.7 billion compared with $13.55 billion in the existing plan.

Implied recoveries, as a percent of total GO/PBA claims of $18.413 billion, show blended GO/PBA recoveries ranging between 57.7% and 58.4%, down from 73.6% in the existing plan. The "discount to POA" as a percentage would range from 22.3% to 20.6%, while the discount in cash would represent a decrease of between $3.025 billion and $2.797 billion.

PSA Creditors' Counterproposal

In an Aug. 24 counterproposal that responds to the "economic reality" caused by the Covid-19 pandemic, the PSA creditors propose upfront cash consideration of $5.984 billion as well as other adjustments starting with a reduction in maximum annual debt service to $1.05 billion for fiscal 2020 and fiscal 2021 and then $1.197 billion for fiscal 2022 to fiscal 2044. Half of the new debt would be GO bonds and half would be COFINA second lien bonds with 25-year terms and a deemed issuance date of March 1, 2020.

The PSA creditor document includes the following summary of their revised proposal:

PROPOSED REVISED PSA ($MM)

In response to the economic reality caused by the pandemic, PSA creditors propose the following adjustments to the PSA

CW Consideration Available for GO / PBA Bondholders

	February 9, 2020 PSA	July 30 FOMB Proposal	August 24 PSA Creditors Proposal
Assumptions			
Annual Debt Service	$1,472	$1,050	FY20-FY21: $1,050 FY22-FY44: $1,197
Debt Service as a % of Own-Source plus COFINA Revenues[1]	8.8%	6.8%	7.8%
Term / Years of Cash Flow	20 Years	20 Years	25 Years
Deemed Issuance Date	3/1/2020	7/1/2021	3/1/2020
True Interest Cost	5.548%	4.135% - 4.811%	5.548%
Duration	7.2 Years	6.8 - 6.9 Years	7.7 Years
Consideration Summary			
Total Debt[2]	$10,669	$4,993 - $5,220	$7,406
Cash Consideration	3,809	5,984	5,984
5.5% Pledged SUT Equity[3]	N/A	N/A	611
Total CW Consideration	**$14,478**	**$10,976 - $11,204**	**$14,001**
Less: CW Consideration to Non-GO / PBA Creditors	(527)	(50)	(50)
Less: PSA Fee and Consummation Costs	(400)	(400)	(400)
CW Consideration Available for GO / PBA	**$13,551**	**$10,526 - $10,754**	**$13,551**
Implied Recoveries			
GO / PBA Blended Recovery (Claims Net of OID)[4]	73.6%	57.2% - 58.4%	73.6%
GO / PBA Blended Recovery (Claims Gross of OID)[5]	72.2%	56.1% - 57.3%	72.2%

(1) PSA calculated based on FY2019 own-source plus COFINA revenues per the May 9, 2019 Certified Fiscal Plan. Proposals calculated based on FY2020 own-source plus COFINA revenues per the May 27, 2020 Certified Fiscal Plan adjusted for actual General Fund revenues per Hacienda.
(2) Under the July 30 FOMB proposal, split between COFINA Jr. and GO bonds is to be determined. Coupon structure to be determined.
(3) Represents net present value as of July 1, 2020 using a discount rate of 20% and the projected 5.5% Pledged SUT implied by the May 27, 2020 Certified Fiscal Plan.
(4) Recoveries based on total GO / PBA claims (net of OID) of $18,413 million.
(5) Recoveries based on total GO / PBA claims (gross of OID) of $18,757 million.

As reflected above, the PSA parties' proposal contemplates a "contingent value instrument" in the form of a 20-year equity security of the 5.5% pledged sales-and-use tax, or SUT. The 5.5% SUT equity would receive 50% of the difference between the actual 5.5% pledged SUT collections and 80% of the 5.5% pledged SUT implied by the May 2020 certified fiscal plan base case. The 5.5% SUT equity would terminate on July 1, 2040, with no further payment obligations under the counterproposal, which establishes that the commonwealth cannot change the scope and amount of the 5.5% pledged SUT and may not exempt goods from the 5.5% pledged SUT without providing for substitution of

collateral of equal value.

"The recoveries to creditors under this proposal maintain the same relative step down negotiated among creditors as under the existing PSA," according to the counterproposal, adding that after accounting for stepdowns among classes, all parties receive their pro rata share of total distributable value to GO and PBA bondholders less $1.073 billion for PBA's administrative claim and $400 million of PSA restriction fee and consummation costs. The PSA creditors' proposal contemplates a revised PSA to include provisions to "protect creditors against renegotiation" and says the "mechanics" of a new PSA would be "negotiated with new milestones and covenants."

Outlining the key benefits of their counterproposal, the PSA creditors say the $1.05 billion cap on debt service through fiscal 2021 would "provide immediate relief" post-pandemic, adding that their plan would reduce nominal debt service by $4.6 billion relative to the existing PSA. They note that payments to the 5.5% SUT equity are variable and "automatically provide[] the commonwealth relief" if risks to the certified fiscal plan materialize. Finally, the counterproposal significantly improves pro forma credit metrics relative to comparable mainland states, according to the PSA creditors.
